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MONTANA LOTTERY

FINANCIAL STATEMENTS
(Unaudited)

September 30, 2011

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MONTANA LOTTERY

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(Unaudited)

September 30, 2011

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APPOINTIVE OFFICIALS

Angela Wong, Lottery Director

John Tarr, Lottery Assistant Director for Security

LOTTERY COMMISSION		TERM EXPIRES
Tom Keegan	Helena	January 1, 2014
Beth O'Halloran	Missoula	January 1, 2014
Wilbur Rehmann	Helena	January 1, 2013
Craig Anderson	Glendive	January 1, 2013
Leo Prigge	Butte	January 1, 2015

REPORT DISTRIBUTION

According to Section 23-7-202(9), MCA, copies of this report must be distributed to the following:

Governor – Brian Schweitzer
Director of Dept. of Administration – Janet Kelly
Legislative Auditor – Tori Hunthausen
President of the Senate – Jim Peterson
Speaker of the House – Mike Milburn

The law also states "the President of the Senate and the Speaker of the House will determine the report distribution to each member of the appropriate committee of each house of the legislature". The President of the Senate and the Speaker of the House have requested that this report be distributed to the following committees:

HOUSE – State Administration Committee

Pat Ingraham, Chair
Gerald Bennett, Vice Chair (R)
Franke Wilmer, Vice Chair (D)
Bryce Bennett
Joanne Blyton
Pat Connell
Betsy Hands
Gordon Hendrick
Douglas Kary
Dan Kennedy
James Knox
Gary MacLaren
Tom McGillvray
Jean Price
Derek Skees
Frank Smith
Kathy Swanson
Ted Washburn

HOUSE – Business & Labor Committee

Elsie Arntzen, Chair
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Chuck Hunter, Vice Chair (D)
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Christy Clark
Virginia Court
Lila Evans
Tim Furey
Edward Greef
Harry Klock
Jonathan McNiven
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Scott Reichner
Michele Reinhart
Matthew Rosendale
Daniel Salomon
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Carolyn Squires
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Ron Arthun, Vice Chair (R)
Jonathan Windy Boy, Vice Chair (D)
Joe Balyeat
Anders Blewett
Larry Jent
Llew Jones
Carmine Mowbray

SENATE – Business, Labor, & Economic Affairs Committee

Joe Balyeat, Chair
Verdell Jackson, Vice Chair (R)
Mitch Tropila, Vice Chair (D)
Tom Facey
Eric Moore
Carmine Mowbray
Donald Steinbeisser
Sharon Stewart-Peregoy
Bruce Tutvedt
Gene Vuckovich
Jonathan Windy Boy

Montana LOTTERY
For the fun of it! 2525 N. Montana, Helena, MT 59601 • P: 406-444-5825 • F: 406-444-5830

December 2011

Montana Lottery Commission:

The past quarter has been an active one. We have had a busy fall with our football events, our planning for the upcoming changes in Powerball, and the new EZ Play games which were rolled out at the beginning of November.

We are off to a good start for the year in game sales. Scratch, Montana Cash, and Mega Millions sales each experienced an increase over last first quarter. Scratch sales were 0.5% higher, Montana Cash was 21.4% higher, and Mega Millions sales were up by 46.5%.

The rest of the games have seen a decreases compared to last year at this time. Powerball sales were 5.7% lower, Wild Card sales were 20.7% lower, Hot Lotto sales were 16.5% lower, and 10 Spot sales dropped by 3.6%.

Overall, there was a slight increase in operating revenue of 0.1% along with an increase in direct game costs of 1.4%. Combined with a 14.4% decrease in operating expenses, the transfer for the first quarter was $2,369,264, which is $117,983 more than last year at this time. The percentage of transfer to revenue was 21.6% this quarter compared to 20.6% last year's first quarter.

The Lottery plans to introduce 40+ new scratch games during the fiscal year 2012. We plan to continue building scratch sales through innovative game themes and offering games with built-in name recognition (licensed property games).

We are looking forward to a busy fall/winter with another season of Fantasy Football and Montana Millionaire along with our new games.

Sincerely,

Angela Wong
Director

MONTANA LOTTERY
STATEMENT OF NET ASSETS
SEPTEMBER 30, 2011 AND 2010
(Unaudited)

	Period Ended September 30, 2011	Period Ended September 30, 2010
ASSETS:		
CURRENT ASSETS		
Cash and Cash Equivalents	$ 2,659,612	$ 1,713,911
Receivables (Net)	1,578,699	1,864,174
Inventories	442,577	597,032
Inventories - Work in Process	598,000	0
Other Current Assets	0	67,623
TOTAL CURRENT ASSETS	5,278,888	4,242,740
NONCURRENT ASSETS		
Computer, Furniture & Equipment	2,487,266	1,159,933
Leasehold Improvements	45,448	45,448
Accumulated Depreciation	(825,309)	(394,752)
Multi-State Reserve fund	1,602,439	1,434,792
TOTAL NONCURRENT ASSETS	3,309,844	2,245,421
TOTAL ASSETS	$ 8,588,732	$ 6,488,161
LIABILITIES:		
CURRENT LIABILITIES		
Accounts Payable	$ 505,393	$ 244,979
Estimated Prize Liability	1,642,136	2,031,533
Due to Primary Government	38	34,739
Transfer Obligations	2,369,264	2,251,281
Deferred Revenue	241,928	194,011
Compensated Absences	110,841	96,328
TOTAL CURRENT LIABILITIES	4,869,600	4,852,871
NONCURRENT LIABILITIES		
MUSL Prize Liability	1,471,394	1,227,146
Compensated Absences	69,629	108,283
Leases Payable	342,797	0
OPEB Liability	398,855	299,861
TOTAL NONCURRENT LIABILITIES	2,282,675	1,635,290
TOTAL LIABILITIES	7,152,275	6,488,161
NET ASSETS		
Unrestricted Net Assets	1,436,457	0
TOTAL NET ASSETS	1,436,457	0
TOTAL LIABILITIES AND NET ASSETS	$ 8,588,732	$ 6,488,161

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
FOR THE QUARTERS ENDED SEPTEMBER 30, 2011 AND 2010
(Unaudited)

	Quarter Ended September 30, 2011	Quarter Ended September 30, 2010
OPERATING REVENUES:		
Scratch ticket revenue	$ 3,786,060	$ 3,766,072
Powerball revenue	3,577,626	3,792,156
Montana Cash revenue	1,226,483	1,010,393
Wild Card revenue	470,679	593,657
Hot Lotto revenue	832,207	996,766
Mt. Sports Action revenue	745	825
Mega Millions revenue	866,399	591,544
10 Spot revenue	187,567	194,573
License, permits, and misc	5,523	413
Total Operating Revenues	10,953,309	10,946,399
Less Direct Game Costs:		
Scratch ticket prize expense	2,452,524	2,197,191
On-line ticket prize expense	3,552,751	3,624,636
Retailer commission	641,152	667,708
Cost of tickets sold	303,029	318,142
Vendor fees	651,906	686,294
Total Direct Game Costs	7,601,362	7,493,971
Income Before Operating Expenses	3,351,947	3,452,428
OPERATING EXPENSES:		
Advertising	212,187	210,469
Advertising Production	35,415	117,255
Audit Fees	3,663	5,031
Bad Debts Expense	(278)	0
Communications	30,252	36,212
Contractual Services	26,379	49,363
Depreciation and Amortization	100,104	43,084
Administrative Service Fee	15,837	27,788
Multi-State Dues	32,110	0
Public Relations	22,506	52,883
Other	18,209	10,393
Personal Services	440,904	452,679
Repairs and Maintenance	9,902	5,495
Supplies and Materials	1,807	104,247
Travel	16,849	26,780
Utilities and Rent	63,853	61,300
Total Operating Expense	1,029,699	1,202,979
Operating Income	2,322,248	2,249,449
NONOPERATING REVENUES (EXPENSES)		
Interest earnings	1,630	1,832
Total Nonoperating Revenues(Expenses)	1,630	1,832
Income Before Operating Transfers	2,323,878	2,251,281
Operating Transfers Out - General Fund	(2,369,264)	(2,251,281)
Total Operating Transfers Out - General Fund	(2,369,264)	(2,251,281)
CHANGE IN NET ASSETS	(45,386)	0
Total Net Assets, Beginning of Period	1,481,843	0
TOTAL NET ASSETS, END OF PERIOD	$ 1,436,457	$ 0

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN NET FUND ASSETS
AND RECONCILIATION OF BUDGET AND ACTUAL (BUDGETARY BASIS) TO GAAP BASIS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2011
(Unaudited)

	Budget Fiscal Year July 1, 2011 - June 30, 2012	Actual Three Months Ended September 30, 2011 (Unaudited)	Actual as a Percent of Final Budget (%)
REVENUES:			
Scratch ticket revenue	$ $15,300,000	$ 3,786,080	24.75
Powerball revenue	14,500,000	3,577,626	24.67
Montana Cash revenue	3,800,000	1,226,483	32.28
Wild Card revenue	2,200,000	470,679	21.39
Hot Lotto revenue	3,800,000	832,207	21.90
MT Millionaire	2,300,000	0	0.00
MT Sports Action (Admin Fees)	5,000	745	14.90
10 Spot	750,000	187,567	25.01
Mega Millions	2,850,000	866,399	30.40
License, permits, and miscellaneous	10,000	5,523	55.23
Total Revenues	45,515,000	10,953,309	24.07
DIRECT GAME COSTS:			
Prizes - Scratch ticket	9,516,600	2,452,524	25.77
Prizes - Lotto games	13,950,000	3,552,751	25.47
Prizes - MT Millionaire	1,460,000	0	0.00
Retailer commissions	2,275,000	641,152	28.18
Ticket cost - scratch games	910,000	303,029	33.30
Ticket cost - vendor fees	2,810,000	651,906	23.20
Total Direct Game Costs	30,921,600	7,601,362	24.58
OPERATING EXPENSES:			
Advertising	615,230	212,187	34.49
Advertising Production	170,000	35,415	20.83
Audit Fees	106,980	3,663	3.42
Communications	142,031	30,252	21.30
Contractual Services	136,589	26,379	19.31
Interest	17,809	0	0.00
Administrative Service Fee	63,348	15,837	25.00
Multi-State Dues	41,350	32,110	77.65
Public Relations	50,000	22,506	45.01
Other	70,419	18,209	25.86
Personal Services	1,800,101	440,904	24.49
Repairs and Maintenance	89,250	9,902	11.09
Supplies and Materials	242,716	1,807	0.74
Travel	49,450	16,849	34.07
Utilities and Rent	231,086	63,853	27.63
Total Operating Expenses	3,826,359	929,873	24.30
Operating Income	10,767,041	2,422,074	22.50
NONOPERATING REVENUES (EXPENSES):			
Interest Earnings	10,000	1,187	11.87
NET INCOME (BUDGETARY BASIS)	$ 10,777,041	$ 2,423,261	22.49
RECONCILIATION OF BUDGETARY/GAAP BASIS:			
Capitalized equipment purchases	48,000	0	0.00
Adjustment for depreciation expense	(400,416)	(100,104)	25.00
MUSL interest earnings	1,500	443	29.53
Total Reconciling Items	(350,916)	(99,383)	
NET INCOME (GAAP BASIS)	$ 10,426,125	$ 2,323,878	22.29

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY

ANALYSIS OF REVENUES AND EXPENSES BY PRODUCT

FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2011

(Unaudited)

	SCRATCH	POWERBALL	MONTANA CASH	WILD CARD	HOT LOTTO	MT. MILLIONAIRE	MEGA MILLIONS	10 SPOT	MT SPORTS ACTION	ADMIN
REVENUES:	$ 3,786,080	$ 3,577,626	$ 1,226,483	$ 470,679	$ 832,207	$ 0	$ 866,399	$ 187,567	$ 745	$ 5,523
DIRECT GAME COSTS:										
Prize Expense	2,452,524	1,724,755	646,941	248,524	400,916	0	423,719	106,546	0	1,350
Retailer Commissions	282,963	178,923	61,353	23,546	41,632	0	43,344	9,389	0	0
Cost of Tickets Sold	303,029	0	0	0	0	0	0	0	0	0
Vendor Fees	219,878	214,881	74,232	30,207	51,870	0	49,881	10,977	0	0
NET OPERATING REVENUE	527,686	1,459,067	443,957	168,400	337,789	0	349,455	60,655	745	4,173
OPERATING EXPENSES:										
Advertising	12,455	21,707	9,481	9,481	9,481	0	121,086	9,481	9,233	9,782
Advertising Production	6,375	6,375	2,361	2,361	2,361	0	6,728	6,375	2,479	0
Audit Fees	0	0	0	0	0	0	0	0	0	3,883
Bad Debts	0	0	0	0	0	0	0	0	0	(278)
Communications	13,072	0	0	0	0	0	0	0	0	17,180
Contractual Services	1,385	6,638	0	0	0	343	0	0	2,451	15,562
Depreciation and Amortization	19,020	9,009	9,009	7,007	7,007	9,009	3,003	3,003	12,012	22,025
Interest	0	0	0	0	0	0	0	0	0	0
Administrative Service Fee	3,959	1,584	1,425	1,109	1,109	950	475	475	950	3,801
Multi-State Dues	0	19,032	0	3,128	5,240	0	4,711	0	0	0
Public Relations	3,124	605	605	605	605	0	605	605	0	15,752
Other	745	0	0	0	0	0	0	0	0	17,464
Personal Services	110,226	44,090	39,681	30,863	30,863	26,454	13,227	13,227	26,454	105,817
Repairs and Maintenance	0	0	0	0	0	0	0	0	0	9,902
Supplies and Materials	20,955	30	30	30	30	0	0	0	0	(19,288)
Travel	5,937	1,475	1,477	1,477	1,477	0	0	0	0	5,035
Utilities and Rent	310	78	78	78	78	0	78	78	0	63,075
TOTAL OPERATING EXPENSES	197,533	110,624	64,147	56,139	58,251	36,756	149,913	33,244	53,579	269,512
OPERATING INCOME	330,153	1,348,463	379,810	112,261	279,538	(36,756)	199,542	27,411	(52,834)	(265,339)
NONOPERATING REVENUES (EXPENSES)										
Security Lending Transactions	0	0	0	0	0	0	0	0	0	0
Interest Earnings	0	0	0	0	0	0	0	0	0	1,630
Gov FA Disp Proceeds	0	0	0	0	0	0	0	0	0	0
Gain(Loss) on Sale of Asset	0	0	0	0	0	0	0	0	0	0
OPEB Expenses	0	0	0	0	0	0	0	0	0	0
TOTAL NONOPERATING REVENUES (EXPENSES)	0	0	0	0	0	0	0	0	0	1,630
NET INCOME BY PRODUCT	$ 330,153	$ 1,348,463	$ 379,810	$ 112,261	$ 279,538	$ (36,756)	$ 199,542	$ 27,411	$ (52,834)	$ (263,709)
PROFIT AS A % OF REVENUE	8.72%	37.69%	30.97%	23.85%	33.59%	0.00%	23.03%	14.61%	N/A	N/A

NOTE: THIS IS THREE MONTHS' ACTIVITY AND THEREFORE SHOULD NOT BE INTERPRETED TO SHOW HOW OUR PRODUCTS HAVE PERFORMED IN PAST YEARS OR WILL PERFORM IN THE FUTURE.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity.

The Montana Lottery, established under the provisions of Section 23-7-101, Montana Code Annotated (MCA), was approved by the Montana electorate through Legislative Referendum No. 100 on November 4, 1986.

Montana's first lottery tickets went on sale June 24, 1987.

The Montana Lottery is operated by a five-member commission consisting of Montana residents appointed by the Governor. The Commission, by law, has the power to operate a state lottery, determine the types and forms of lottery games, set the ticket price, number and size of prizes, conduct lottery drawings, enter into agreements to offer lottery games in conjunction with other lottery states and countries, and prepare financial reports. The Montana Lottery is attached to the Montana Department of Administration for administrative purposes.

The Montana Lottery is included as an enterprise fund in the State of Montana's Comprehensive Annual Financial Report. In accordance with governmental accounting and financial reporting standards, there are no component units to be included within the Montana Lottery's financial statements as a reporting entity.

Basis of Presentation. The Montana Lottery reports its financial activity in accordance with generally accepted accounting principles (GAAP) as prescribed in pronouncements of the Governmental Accounting Standards Board (GASB).

Enterprise Fund. The Montana Lottery is classified as an Enterprise Fund of the Proprietary Fund Type. Enterprise Funds account for operations: a) financed and operated similar to private business enterprises, where the intent of the Legislature is that costs are to be financed or recovered primarily through user charges, or b) where the Legislature has decided that periodic determination of revenue earned, expenses incurred, or net income is appropriate.

Basis of Accounting. The Montana Lottery's financial statements are prepared using the accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and become measurable; expenses are recognized in the period incurred, if measurable.

Property and equipment. Property and equipment are recorded at cost. Donated property and equipment are recorded at their estimated fair market value at the date of donation. Ordinary maintenance and repairs are charged to operations as incurred; major renewals and betterments are capitalized. Upon disposition or retirement of property and equipment, the cost and related accumulated depreciation or amortization are removed from the accounts. Gain or loss on disposal is reflected in non-operating revenues and expenses. Depreciation and amortization are calculated on a straight-line basis over estimated useful lives of three to ten years. The Lottery conforms to the State of Montana capitalization threshold for capitalizing property and equipment as well as buildings and building/land improvements. The threshold for capitalizing property and equipment is $5,000 and the threshold for capitalizing buildings/land improvements is $25,000.

Revenue Recognition. Lottery scratch ticket sales are recorded as revenue based on the time the retailer activates the pack of tickets for sale. In accordance with an established policy, retailers may return unsold tickets to the Lottery for credit. Sales are decreased by an allowance for estimated ticket returns.

Ticket sales for lotto games Powerball, Wild Card, Montana Cash, Hot Lotto, Montana Millionaire, Mega Millions, and 10 Spot are recorded as revenue based on drawings. Tickets sold in advance for future drawings are recorded as deferred revenue until such time as the tickets become valid for the most current drawing.

Ticket sales for Fantasy Sports games are based upon MCA 23-4-302 and an interagency agreement between the Lottery and the Board of Horse Racing.

Classification of Revenues. The Lottery has classified its revenues as either operating or non-operating according to the following criteria:

Operating revenues – include activities that have characteristics of exchange transactions, including (1) ticket sales, net of returns, and (2) retailer license fees and administrative fees in relation to selling lottery tickets.

Non-Operating revenues – include activities that have the characteristics of non-exchange transactions, such as gifts and other revenue sources that are defined as non-operating revenues by GASB No. 9, "Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting," and GASB No. 34, "Basic Financial Statements and Management Discussion and Analysis for State and Local Governments." Types of revenue sources that fall into this classification are state appropriations, investment income, and gain or loss on disposition of assets.

Free Tickets. Some Montana Lottery scratch games award free tickets as prizes. Net lottery ticket revenue does not include the value of free tickets given away and free plays won. The face value of these free ticket prizes distributed for the quarter ended September 30, 2011 was $102,396.

Promotional Credits. The Lottery issues promotional credits to retailers to be used to distribute free tickets to players. The tickets are distributed as part of a promotion run by the retailer, e.g., "Ask for the Sale" or second chance drawings. The Lottery also directly distributes scratch tickets for promotional purposes at trade shows, for media give-aways, and during new game introductions. The tickets distributed as a result of promotional credits are reflected as a reduction in revenue. The related prize expense and ticket cost for all promotions are reclassified as an advertising expense. For the quarter ended September 30, 2011, promotional credits resulted in a revenue reduction of approximately $9,404 and an expense reclassification of approximately $6,860.

Prizes. Expenses for scratch prizes are recorded based on the predetermined prize structure for each game. Expenses for lotto prizes are recorded based on the predetermined prize structure for each individual game. No prize expense is recorded for free tickets distributed.

Unclaimed Prizes. Prizes for the lotto games must be claimed within six months after the appropriate draw date. Prizes for scratch games must be claimed within six months of the announced end of each game. The unclaimed prize amounts for the Montana Lottery lotto games are taken as a reduction in the Lottery Prizes Payable liability and the Prize Expense and are transferred to the State of Montana General Fund as a portion of the quarterly transfer. The amount of unclaimed prizes for all Montana Lottery games is represented in the table below.

	Quarter Ended 9/30/11	Quarter Ended 9/30/10	Year To Date 9/30/11	Year To Date 9/30/10
Lotto	$117,521	$104,500	$117,521	$104,500
Scratch	$ 0	$240,786	$ 0	$240,786
TOTALS	$117,521	$345,286	$117,521	$345,286

2. SUMMARY OF ACCOUNTS

Cash and Cash Equivalents. Cash and cash equivalents consist of interest-bearing deposits with the Montana Board of Investments short-term investment pool, cash on deposit in revolving account with a non-state financial institution and cash on deposit with the Montana State Treasurer that is part of the State's pooled cash and is not separately identifiable as to specific types of securities. These funds are highly liquid and may be drawn on daily.

Cash and cash equivalents consist of the following:

	September 30,	
	2011	2010
Short-term investment pool	$2,493,730	$1,086,157
Cash on deposit with State Treasurer	155,882	617,604
Cash in revolving deposit account	10,000	10,000
Petty Cash & Cash on Hand	0	150
TOTALS	$2,659,612	$1,713,911

The bank balance of the revolving deposit account, not including outstanding deposits or checks, was $12,066 at September 30, 2011 and was covered by federal depository insurance. The carrying amount reported in the balance sheet for cash and cash equivalents approximates the fair market value.

Receivables. Receivables include $1,822,122, representing amounts due the Lottery for tickets purchased by retailers. An allowance for ticket returns is included in the receivables amount. This allowance represents a reduction in receivables at September 30, 2011, for estimated ticket returns. This is an estimate based on returns received to date, as well as an estimate of tickets unsold by retailers for games that have a public sale end date prior to October 1, 2011. The allowance for ticket returns is $258,411 at September 30, 2011. The return of vendor fees related to the allowance for returns is $14,988.

Inventories. Inventories consist of merchandise and supplies inventories. Merchandise inventory includes scratch tickets valued at $366,187 stored in the warehouse, at retailers prior to being activated by the retailer, and with the marketing representatives. These ticket inventories are recorded at cost using the specific identification method and maintained on a perpetual inventory system. Tickets are charged to cost of tickets sold upon activation or after game end.

Supplies inventories include ticket dispensers, premiums and point-of-sale materials. At year end, supplies inventories totaled $76,390. These inventories are also recorded at cost using the specific identification method.

Property and Equipment. A summary of property and equipment for the Lottery is as follows:

	June 30, 2011	Additions	Deletions	September 30, 2011
Leasehold Improvements	$ 45,448	$ -	$ -	$ 45,448
Furniture & Equipment	$ 2,415,766	$ 71,500	$ -	$ 2,487,266
Accumulated Depreciation	$ (725,205)	$(100,104)	$ -	$ (825,309)

Receivable – Equipment. The equipment receivable by the Lottery of $1,625,000 was for 250 on-line vending machines due from the Lottery's primary vendor on June 30, 2010.

Other Current Assets. Other current assets include the following:

	September 30, 2011	2010
Prepaid Expenses	$ -	$67,623
Employee Advances	-	-
TOTALS	$ -	$67,623

The prepaid expense amount for September 30, 2010 consists of $67,623 for the remaining two truck prizes.

Transfer Obligations. The account "Transfer Obligations" is $2,369,264 payable to the General Fund at September 30, 2011.

Compensated Absences. State employees earn vacation leave ranging from 15 to 24 days per year depending on the individual's years of service. Vacation leave may be accumulated not to exceed two times the maximum number of days earned annually. With no limit on accumulation, sick leave is earned at 12 days per year. Upon retirement or termination, an employee is paid 100% for unused vacation and 25% for unused sick leave. The Lottery's liability for compensated absences is detailed below.

Balance June 30, 2011	Net Leave Earned/(Used)	Balance September 30, 2011
$199,169	$(18,699)	$180,470

Commissions. Section 23-7-301(10), MCA, provides retailers a commission on scratch and lotto tickets or chances sold. The Lottery Commission established this commission at 5% of the face value of scratch tickets activated by the retailers and the face value of lotto tickets sold. Section 23-4-302 (5)(b)(i), MCA establishes a 3.99% commission of the face value of Fantasy Sports tickets sold. In addition retailers can earn bonus commissions on tickets sold based on incremental sales of scratch tickets. For the quarter ended September 30, 2011 retailers earned bonus commissions of $89,418. For the quarter ended September 30, 2011 total commissions were $641,152.

OPEB (Other Post Employment Benefits) Implicit Rate Subsidy LT. Effective for Fiscal Year End 08, GASB Statement 45 and the reporting requirements for the "implied rate subsidy" required the State of Montana to book substantial liabilities. The liability is a result of the state's requirement to allow retired employees to remain in the retirement plan after retirement. This results in an implicit rate subsidy since retirees pay the same amount as active employees. "Actuaries Northwest" prepared the report for the State of Montana to calculate the Annual Required Contribution under the Governmental Accounting Standards Board (GASB). The allocation is made based on the fiscal year's benefits expense and the number of full time employees for an agency.

The Lottery's OPEB obligations for 2011 and 2010 are as follows:

Year ended June 30,	2011	2010
Annual Required Contribution	$ 98,994	$ 83,673
Adjustment to annual required contributions	-	-
Annual OPEB cost	$ 98,994	$ 83.673
Contributions made	-	-
Increase to net OPEB obligation	$ 98,994	$ 83,673
Net OPEB obligation – beginning of year	$ 299,861	$ 216,188
Net OPEB obligation – end of year	$ 398,855	$ 299,861

3. PAYMENTS TO OTHER STATE AGENCIES

The Lottery receives a variety of services, supplies, and materials from other state agencies. These services and materials are detailed below for the fiscal year ended September 30, 2011:

Insurance	$ 2,136
Warrant Writing Services	66
Payroll Services	1,878
Audit Fees	3,443
Computer Fees	5,347
State Accounting System Support	762
Supplies & Materials	2,893
Mail Processing Fees	5,102
Telecommunications	7,508
Administrative Service Fees	15,837
Other	64
TOTAL	$ 45,036

4. PRIZES

Paid Prizes. Section 23-7-402, MCA states, "A minimum of 45% of the money paid for tickets or chances must be paid as prize money". Prize expense is recorded based on the predetermined prize structure percentage for each game less unclaimed prizes. For the quarter ended September 30, 2011, the prize expense of $6,005,275 is 54.86% of net Lottery ticket revenue of $10,947,041.

5. TRANSFER TO STATE GENERAL FUND

Section 23-7-402(3), MCA, states "That part of all gross revenue not used for payment of prizes, commissions, and operating expenses, together with the interest earned on the gross revenue while the gross revenue is in the enterprise fund, is net revenue. Net revenue must be transferred quarterly from the enterprise fund established by 23-7-401 to the State General Fund." For the quarter ended September 30, 2011, the net revenue payable to the State General Fund totaled $2,369,264

6. MULTI-STATE LOTTERY

In November 1989 the Montana State Lottery joined the Multi-State Lottery Association (MUSL). MUSL was created in September 1987 to operate a multi-state lottery game for the benefit of party lotteries. Powerball, Wild Card, Hot Lotto, and Mega Millions are the games jointly operated by the members, in which Montana presently participates. Each lottery participating in MUSL is represented on the Board of Directors.

The Multi-State Lottery Reserve Fund with a balance of $1,602,439 as of September 30, 2011 is comprised of several reserve accounts, which are maintained by the Multi-State Lottery Association (MUSL). The balance of these reserve accounts is as follows:

	September 30, 2011	September 30, 2010
Powerball Prize Reserve Account	$ 682,526	$ 518,311
Powerball Set Prize Reserve Account	170,632	166,199
Powerball Unreserved Account	131,045	207,645
Wild Card Prize Reserved Account	210,493	238,924
Hot Lotto Set Prize Reserve Account	354,887	315,126
Mega Millions Prize Reserve Account	52,856	(11,413)
Total	$1,602,439	$1,434,792

The Powerball Prize Reserve Account is to be used only in the event of an unanticipated prize claim. It is an insurance fund intended to protect the member lotteries against the liability that could result from a system failure at one of the member lotteries. All money paid to this fund would be returned to the Lottery one year after the Lottery leaves the Powerball game, assuming that no unanticipated prize claims have been paid. Interest earned on the Lottery's share of the fund, represented by the Unreserved Account, would be returned to the Lottery upon leaving MUSL. The amounts in the Unreserved Account may be used at the MUSL Board's discretion.

The Powerball Set Prize Reserve Account is used to fund prize payments for current drawings. Since the Powerball game has fixed prizes, it is often necessary to draw from this reserve to fund payment of prizes at the fixed amount. This account would be returned to the Lottery upon withdrawal from the Powerball Game.

The Lottery contributes to these reserve funds through the 50% set aside for prizes. In addition the Lottery was required to contribute for its portion of the reserve funds accumulated since the start of the Powerball game. Payments made to this fund are considered a portion of prize expense associated with the game.

The Wild Card Reserve Account is to be used in the event of an unanticipated prize claim on the Wild Card game. This account is also administered by MUSL and would be returned to the Lottery one year after the Wild Card Product Group of Idaho, Montana, South Dakota, and North Dakota is disbanded. The Lottery contributes to this account through the 55% set aside for prizes. Payments made to this fund are considered a portion of prize expense related to the Wild Card game.

The Hot Lotto Set Prize Reserve Account is administered by MUSL and is to be used only in the event of unanticipated prize claims. Like other MUSL games the reserve amount would be returned to the Lottery one year after withdrawal from the Hot Lotto game. The Lottery contributes to the reserve through the 50% set aside for prizes. Payments made to the reserve are considered a portion of the prize expense related to the game.

The Mega Millions Prize Reserve Account is to be used only in the event of an unanticipated prize claim. It is an insurance fund intended to protect the member lotteries against the liability that could result from a system failure at one of the member lotteries. All money paid to this fund would be returned to the Lottery one year after the Lottery leaves the Mega Millions game, assuming that no unanticipated prize claims have been paid. The Lottery contributes to the reserve through the 51% set aside for prizes. Payments made to the reserve are considered a portion of the prize expense related to the game. The Lottery had just started cross-selling Mega Millions during the fiscal year end 2010. As a start-up game, the reserve was negative at the year end as the Lottery had not built up enough history and accumulated enough sales to create an excess reserve.

7. GAMES

Currently, the Montana Lottery games are scratch ticket games, seven lotto games referred to as Powerball, Montana Ca$h, Wild Card, Hot Lotto, Mega Millions, 10 Spot, and Montana Millionaire, a limited edition lottery game. The lottery is facilitating Fantasy Sports Games on behalf of the Board of Horse Racing. Currently the Lottery is selling the Montana Sports Action Fantasy Football and the Racing games.

Scratch ticket games provide players the opportunity to win instantly by scratching latex covering to reveal a prize.

The Powerball game allows players the chance to win a minimum pari-mutuel jackpot of approximately $20 million. A player must match all 6 numbers to win the jackpot; players win prizes ranging from $3 to $200,000 for matching less than all 6 numbers. Drawings are held twice weekly on Wednesday and Saturday nights. For any drawing, if no ticket matches 6 out of 6 numbers, the jackpot rolls over to the next drawing to create a progressive jackpot. In March 2001, the Lottery added

Power Play to the Powerball game. For an additional bet, the Power Play option provides non-jackpot winners the chance to multiply their prize amount by a factor of two through five.

The Montana Ca$h game allows players the chance to win a minimum pari-mutuel jackpot of $20,000. Players select 5 numbers from a field of 37 and must match at least 3 out of 5 to win a prize. Matching 3 of 5 wins $5 and 4 of 5 wins $200. The drawing is conducted twice weekly on Wednesday and Saturday nights. If no ticket matches all 5 numbers, the jackpot rolls over to the next drawing to create a progressive jackpot.

The Wild Card game allows players the chance to win a pari-mutuel jackpot, with a guaranteed minimum of $100,000. Players select 5 numbers from a field of 31 plus one of 16 face cards and must match all 5 numbers and the wild card to win the jackpot; players win prizes from $1 to $5,000 for matching less than all 5 numbers and/or the wild card. Drawings are held twice weekly on Wednesday and Saturday nights. If no ticket matches all 5 numbers and the wild card, the jackpot rolls over to the next drawing to create a progressive jackpot.

Hot Lotto allows players the chance to win a pari-mutuel jackpot with a guaranteed minimum of $1 million. Players choose 5 numbers from a field of 39 plus 1 Hot Ball number from a field of 19; the first 5 numbers and the Hot Ball must be matched to win the jackpot. Players can win prizes ranging from $2 to $10,000 by matching less than all 5 numbers and/or the Hot Ball. If no ticket wins the jackpot, it rolls over to the next drawing to create a progressive jackpot. Drawings are held twice weekly on Wednesday and Saturday nights. In January 2008, the Lottery added the Sizzler option to the Hot Lotto game. For an additional bet, the Sizzler option provides non-jackpot winners the chance to multiply their prize amount by three.

Mega Millions is a multi-state game that allows players to win a minimum pari-mutuel jackpot starting at $12 million. Mega Millions went on sale March 1, 2010 in Montana. To win the jackpot, players must match all six numbers drawn; other prizes range from $2 to $250,000. Drawings are held each Tuesday and Friday. Mega Millions has a Megaplier option which multiplies non-jackpot prizes by two, three, or four. The Megaplier options costs $1 extra per play.

10 Spot, which went on sale February 1, 2010, is a Montana-only, twice daily game. Players select ten numbers from one through eighty. The Lottery draws twenty numbers, and players win by matching ten, nine, eight, seven, six, five, or none of the numbers drawn. Prizes range from $2 to $25,000.

Montana Sports Action is a product line introduced by the Lottery in August 2008 on behalf of the Board of Horse Racing. Montana Sports Action Fantasy Football was the first game within the Fantasy Sports Games to begin. Players choose five

eligible offensive players and a defensive unit from the official roster of professional football players and teams, to create their own team. The players then choose a play amount ($5, $10, $20, $50, or $100) which determines the shares the player is eligible to win should their team have one of the three highest point totals for the week.

After completion of each week's professional football games, points are assigned to football players and defensive units based on their performance to determine the Lottery players' team's performance. Prizes paid must be 74% of sales for the week. How much the player wins is determined by their team's points and their share ($5 per share). Ticket sales are allowed each week of the professional football season beginning Tuesday morning for that week's games with no advanced purchasing allowed.

Fantasy Racing was introduced in February 2009, and follows the NASCAR® Sprint Cup Series. Fantasy Racing teams are created by selecting a driver from the top nine-ranked drivers for the week; three drivers ranked from ten through 34; and one driver ranked 35 or above. The sixth element in a player's Fantasy Racing team is the number of yellow-flag cautions the player believes might occur in that week's race. Players also choose the number of shares they wish to buy ($5, $10, $20, $50 or $100). Like Fantasy Football, the number of shares determines the amount of the prize each winning ticket will win. After each Sprint Cup race, points are assigned to each driver's performance, and teams with the top three point totals win. Ticket sales begin each week on Monday.

Montana Millionaire began on November 1, 2009 with the final drawing on January 1, 2010. The tickets were sold sequentially across the state with 1 to 150,000 available. There were 400 - $50 instant win prizes for every 375th ticket purchased. The final drawings were held on January 1, 2010 and consisted of one $1 million dollar top prize, five $100,000 prizes, and five $10,000 prizes. This game will begin again on November 1, 2011 with the final drawing on approximately January 1, 2012. The number of tickets available will be 125,000 with an early bird prize of $10,000 being awarded in late November.

8. COMMITMENTS - GAMING SUPPLIER CONTRACTS

Scratch Tickets. On June 27, 2008 the Montana Lottery Commission approved the award of a five-year contract with Scientific Games International (SGI) for the provision of scratch tickets. The contract is for five years with the option for two additional one-year renewals. The contract contains specifications regarding ticket design, printing, game ownership, inspection, and prize structure.

SGI, as the vendor, provided a performance bond covering the contract term and an errors and omissions policy covering an ultimate net loss of $3,000,000. The Lottery may terminate this contract by providing proper notification to Scientific Games.

On-line Services. On October 11, 2005, the Lottery signed a seven-year contract with Intralot, Inc. of Duluth, GA to provide an on-line gaming system and the associated services beginning March 31, 2006. The contract requires Intralot to provide new terminals to all retailers with the associated software and communications. Payment under the contract is based on 5.8% of net weekly Lottery sales of lotto and scratch games. On August 18, 2008 an addendum was signed to provide services for the Fantasy Sports games at 3% of net weekly Lottery sales up to $2,999,999 of Montana Sports Action games. The contract currently has a termination date of March 30, 2016.

9. LOTTO*AMERICA/POWERBALL/TRI-WEST JACKPOT PRIZES

Jackpot prizes awarded in the Lotto*America/POWERBALL and TRI-WEST LOTTO games are funded through the purchase of U.S. Treasury Zero-Coupon Bonds purchased in the name of the Montana Lottery by MUSL. MUSL will cash the bonds each year as they mature and will wire the funds to the Lottery for payment to winners on the Anniversary date of the win.

On January 13, 1990 the Montana Lottery awarded its first Lotto*America jackpot prize totaling $1,740,000. The first annual payment of $87,000 was made on February 1, 1990. On May 9, 1990 the Lottery awarded a second Lotto*America jackpot prize of $3,000,000. The first annual payment of $150,000 was made on May 23, 1990. A third jackpot prize was awarded on February 2, 1991 for $7,360,000. The first annual payment of $368,000 was made February 15, 1991. On November 23, 1991 a fourth jackpot prize was awarded totaling $46,967,738.57. The first annual payment of $2,355,738.57 was made December 12, 1991. On April 11, 1992 a fifth jackpot prize was won totaling $2,000,000. The first annual payment of $100,000 was made on April 27, 1992.

On July 6, 1994 the Montana Lottery awarded its first Tri-West Lotto jackpot prize totaling $700,565. The first annual payment of $35,000 was made on July 26, 1994.

On July 22, 1995 the Montana Lottery awarded its first Powerball jackpot prize totaling $31,401,655.99. The first payment of $1,571,655.99 was made on August 8, 1995. On April 5, 1997 the Lottery awarded a second Powerball jackpot prize totaling $11,000,000. The first annual payment of $550,000 was awarded on April 18, 1997.

On March 27, 1999 the Montana Lottery had a Powerball jackpot winner. The prize was $35.1 million ($19.35 million cash option). The winner chose the cash option and was paid a lump sum in June 1999.

On June 23, 2010 the Montana Lottery awarded its fourth Powerball jackpot prize. The total jackpot was $96,856,406 and was split between another ticket in Ohio. Half of the jackpot, which was again split between two winners in Montana, totaled $48.5 million (25.08 million cash option). The winners chose the cash option and were paid a lump sum in July 2010.

As of September 30, 2011, the combined total of future prize payments funded through the purchase of U.S. Treasury Zero-Coupon Bonds for Powerball and Tri-West Lotto winners was $7,530,000. Total annual payments due as of September 30, 2011 are as follows:

FYE	
2012	$ 550,000
2013	2,155,000
2014	2,155,000
2015	2,120,000
2016	550,000
	$ 7,530,000

10. LEASES/INSTALLMENT PURCHASES PAYABLE

Rent. The Montana Lottery leases its office, administrative and warehouse facilities under a lease agreement that is effective September 2007 through August 2017. The monthly lease payment is $11,099 through August 2011. The base rate will increase 3% annually.

Capital Lease. The Lottery has contracted with its vendor to lease equipment for the remaining life of its contract with them. Obligations under this capital lease/installment purchase at September 30, 2011 are as follows:

FYE	
2012	$ 89,977
2013	85,827
2014	81,677
2015	77,528
2016	55,423
Total Minimum Payments	390,432
Less: Interest	(47,635)
Present value of Minimum Payments	$ 342,797

11. INVESTMENT RISK DISCLOSURES

Effective June 30, 2005, the State of Montana implemented the provisions of Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures*. The Lottery participates in two investment pools: the Multi-State Lottery Association (MUSL) reserve accounts and the State of Montana's Short Term Investment Pool (STIP). There are four types of risk that must be disclosed. These risks are defined below, followed by their applicability to each of the investment pools.

Multi-State Lottery Association The MUSL investment policy for prize reserve and unreserved funds states that permitted investments "include direct obligations of the United States government, perfected repurchase agreements, and obligations issued or guaranteed as to payment of principal and interest by agencies or instrumentalities of the United States government, and mutual funds of approved investments".

Short-term Investment Pool All short-term funds are held in the State's Short Term Investment Pool (STIP) administered by the Board of Investments (BOI). STIP is an external 2a-7 like pool.

Credit risk is defined as the risk that an issuer of an investment will not fulfill its obligation, i.e., not make timely principal and interest payments. The STIP securities have credit risk as measured by major credit rating services, however, the pool is not rated. The Lottery does not have a policy regarding credit risk

Per MUSL, the prize reserves held on behalf of the Montana Lottery are invested in the Montana Winners Trust and include 51% in securities held as obligations of the U.S. Government and are not considered to have credit risk. The other 49% of the prize reserves are invested in Federal Agencies and have an AAA credit quality

rating. The Lottery does not have any authority or a policy regarding the investment portfolios.

Custodial credit risk is the risk that the Lottery would not be able to recover the value of the investment or collateral securities that are in the possession of an outside party in the event of the failure of that party. Custodial credit risk does not apply to STIP because it is a 2a-7 like pool.

The MUSL prize reserves are held in the Montana Winners Trust using policies set forth by the MUSL board regarding policies for the type of securities, as well as the custody, trading and the use of proceeds of the securities. The Lottery does not have any authority or a policy regarding the investment portfolios.

Concentration of credit is the risk of loss attributed to the magnitude of a government's investment in a single issuer. Because STIP is a pooled investment, this risk does not apply. Because the MUSL reserves are also a pooled investment, this risk does not apply to them either.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Interest rate risk does not apply to STIP because it is a 2a-7 like pool.

The MUSL prize reserves are invested through the Montana Winners Trust in the Morgan Stanley Government Portfolio Funds with daily liquidity and therefore have no interest rate risk. The MUSL board's investment policy limits the individual security and the portfolio's maturity. As of June 30, 2010, the duration for the U.S. Government Treasury securities was 1.036 years and for the Agency securities was 0.739 years.

-Alternative accessible formats of this document will be provided upon request.